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COMMERCIAL PAPER AND THE FEDERAL RESERVE BOARD

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In the reform of our banking system provided in the Federal Reserve Act it was recognized that an achievement greatly to be desired was the establishment of an open discount market. For the domestic situation such a market was regarded as essential to the free flow of banking credits from section to section. Internationally an open market to which the foreign banker might be attracted was looked upon as a means of helping to safeguard the national reserves. Furthermore there was unquestionably a general feeling that to an excessive degree our banking resources had been directed toward investment and speculation rather than toward commercial ends, and it was believed to be desirable to correct, if possible, any excessive tendency of this kind. Hence, while the Federal Reserve Act attempts to provide for the kind of commercial paper that would meet the needs of a good discount market, it essays at the same time to exclude from such market the kind of paper that is held to be undesirable.

Section 13 of the act provides for the rediscount at the Federal reserve banks, upon the endorsement of any of its member banks, of "notes, drafts and bills of exchange arising out of actual commercial transactions," but it is left for the Federal Reserve Board to determine the character of the paper thus available for discount. There is express provision, however, for the acceptance for discount of paper based on "staple agricultural products or other goods, wares or merchandise," and there is similarly an express rejection of bills "covering merely investments or issued or drawn for the purpose of carrying or trading in stocks, bonds," etc., except securities issued by the government of the United States. The maturity of bills acceptable for discount is also limited to ninety days although special provision is made for six months' agricultural and live stock paper. Furthermore, specific provision is made for the development of acceptances in the field of exports and imports,

although even in that field limits are imposed on the amounts that a member bank may accept for individuals, firms, etc. and that it may accept *in toto*, while limits are similarly imposed on the reserve banks themselves in their dealings with member banks. The original acceptances by member banks may be of a maturity up to six months, but the rediscounts at the reserve banks are limited to three months' maturity. Finally, in section 14 the act provides that "any federal reserve bank may under rules and regulations prescribed by the Federal Reserve Board" purchase and sell in the open market from or to anybody "cable transfers and bankers' acceptances and bills of exchange" of the kinds and maturities made eligible for rediscount "with or without the indorsement of a member bank."

In other words, as a basis of the projected discount market, the act provides for three kinds of paper as follows: (a) Commercial paper, namely "notes, drafts and bills of exchange arising out of actual commercial transactions," that is paper "issued or drawn for agricultural, industrial or commercial purposes, or the proceeds of which have been used or are to be used for such purposes"; (b) commodity paper, namely paper secured by "staple agricultural products or other goods, wares or merchandise"; and, lastly (c) acceptances growing out of exports and of imports. But while the act itself imposes certain requirements on the paper eligible for rediscount at, or for purchase by, the federal reserve banks, it imposes on the Federal Reserve Board the responsibility of determining in detail the character of such paper.

In view of the peculiar development of American credit methods in the past, there arose, after the passage of the Federal Reserve Act, the liveliest discussion as to the manner in which the Reserve Board should exercise the responsibility thus entrusted to it. Owing to the specific provisions of the act there was no serious difference of opinion about commodity paper and about acceptances growing out of exports and imports. But with respect to the "notes, drafts, and bills of exchange arising out of actual commercial transactions" the discussion waxed warm. The issue was drawn between what is known as "single-name paper" and what on the other hand is known as "double-name paper." There is no occasion in this place for referring to the sundry interesting representations made by both sides. Suffice it to say that the question

involved first, the desirability of including single-name paper at all, and second, assuming a definition of character broad enough to include it, the further question as to whether for discount purposes there should not be a discrimination against single-name paper in favor of double-name paper. In view of the widespread dependence upon single-name paper in the United States, however, there was also much difference of opinion as to whether the two-name system could be successfully propagated here.

In the administration of the Reserve Act this question of commercial paper was one of the first that the Reserve Board had to face, and it is the purpose of this paper to set forth what has been done by the Board in this connection.

In its early deliberations the board was aided by a careful report prepared by a committee of banking experts, headed by Dr. H. Parker Willis, who subsequently became the Secretary of the Board. This committee had been selected by the Reserve Bank Organization Committee to study the whole question of the organization of the reserve banks. It made a scholarly report covering every important question of technique and principle, and, while its report was at first confidential, the Reserve Board reproduced in its own First Annual Report much of the material presented in the confidential report of the committee. Attention here is directed toward what the committee had to say concerning commercial paper.¹

After setting forth clearly the essentials of the question the committee came to the conclusion that it was clearly the intention of Congress to include in the paper eligible for rediscount single-name paper having the prescribed qualifications. It based its conclusion on the fact that the act specifically mentioned not only the instruments the proceeds of which *had been* used for agricultural, industrial and commercial transactions, but also those which were *to be* used for such purposes. A two-name bill assumes a transaction completed; hence a contemplated transaction could hardly give rise in advance to a two-name bill. But the committee pointed out that while single-name paper was to be included there must be no doubt about the use of the proceeds for strictly commercial purposes.

The committee then discussed the means that might be em-

¹ Page 119 *et seq.*

ployed for preventing the use of the proceeds of rediscounted paper for the forbidden purposes of obtaining current capital and of financing speculation. It pointed out that in practice it would be impossible as well as unnecessary to insure the use in the permitted directions of the particular sum advanced by the banks on rediscounted paper as long as there was the assurance that "an equal sum drawn from the liquid resources of the concern receiving the advance is so applied." In other words, according to the committee, it is a question simply as to whether the person or firm getting the advance "is engaged in actual business of the kind referred to and is in liquid condition."² That the committee favored, however, as full a restriction of single-name paper as possible is indicated in the statement that "wherever possible the proportion of single-name paper allowed to figure in the rediscounts of a federal reserve bank should be confined to the lowest basis consistent with the welfare and convenience of the business community."

The committee also suggested several means of accelerating the development of two-name paper and, at the same time, of restricting single-name paper. It looked with favor on a "differential rate" slightly in favor of double-name paper. It suggested the possibility of "restricting the total amount of single-name paper admitted to rediscount to a given percentage of the gross rediscounts of the reserve bank in question."³ Along this same line the committee deemed worthy of mention also that note brokers might be required under certain conditions personally to indorse the single-name paper which they offer for sale to the banks of the reserve system.

At the conclusion of its discussion of this subject the committee summed up its recommendations and enumerated the points that it considered essential in determining the practice of the reserve banks. Single-name paper must of course be considered eligible, but the committee stated that owing to the possibility of using single-name paper for purposes of speculation the responsibility must devolve upon the member banks to see to it that funds originally derived from the sale of single-name paper are properly applied. Furthermore the committee believed that the drawer of single-name paper should secure his financial responsibility by a

² *First Annual Report of the Federal Reserve Board*, p. 253.

³ *Loc. cit.* p. 153.

proper statement and that, when presented for rediscount, his paper should have in addition to the member bank's indorsement a statement signed by an officer of the bank that to his "best knowledge and belief" the proceeds of the paper had been or were to be used for business of a strictly current nature and not for what might be construed as merely an investment.

As to two-name paper the committee believed that by a customary credit statement the responsibility of either maker or endorser should be reasonably assured by the member bank presenting the paper for discount, and, further, that in the original discount the practice ought to be to require that at least one of the parties involved file a statement with the member bank. Lastly the committee recommended separate schedules and statements for the two kinds of paper.

The action taken by the Reserve Board itself in connection with the paper eligible for rediscount and with that eligible for the open market operations of the reserve banks, is to be found in a series of circulars and regulations issued by the board from time to time, as circumstances seemed to demand. In connection with the promulgation of its regulations the board has adopted the happy practice of issuing at the same time an explanatory circular. Hence taking the circulars and the regulations together it is possible to see very clearly what the general attitude of the board really is on the subjects dealt with in the circular.

Two sets of circulars and regulations, dealing with the subject of commercial paper in general have been issued.⁴ A careful comparison of these will disclose the fact that while accepting single-name paper as eligible for rediscount, the board originally proposed a drastic system of control which was, however, considerably modified later on.

In the first circular the board stated that it wished to make both kinds of paper available, but it emphasized the principle that paper representing permanent investments must be excluded. Paper, the board said, should be essentially self-liquidating, and bills would meet this requirement, when they represented "in every case some distinct step or stage in the productive or distributive process—the progression of goods from producer to con-

⁴ Circular No. 13 of 1914 and No. 3 of 1915; Regulations 2 and 4 of 1914 and 3 of 1915.

sumers." In the second circular, which accompanied the modified and more liberal regulations superseding those originally issued, the board stated that it had "not modified its views upon the general principles" which in the earlier circular and regulations had been "expressed as being of fundamental importance in the best development of the new system." In other words, the Reserve Board apparently desired it to be understood that while it was willing to meet the exigencies of the actual situation, it stood its ground on the question of principle.

In the first regulation (No. 2 of 1914), dealing with the question of eligibility, the board points out that the Reserve Act forbids the acceptance for rediscount by the reserve banks of notes, drafts and bills of exchange covering "merely investments." But as any funds employed in agriculture industry and commerce are quasi-investments, the Board held that the significance of the prohibition was to be sought in the word "merely." From this point of view those bills are ineligible whose proceeds have been or are to be used in permanent or fixed forms of any kind. This applies also to paper arising from the purchase of commodities, agricultural or otherwise, when such purchase is merely speculative and is "not connected with an ultimate process of manufacturing or distribution."

In the superseding regulation the board took the same position. Only such bills were considered eligible whose proceeds had been used or were to be used "in producing, purchasing, carrying or marketing goods in one or more of the steps of the process of production, manufacture and distribution." But in this connection the board made a concession. The new regulation provided that "it may be considered a sufficient evidence of compliance . . . if the borrower shows by statement or otherwise that he has a reasonable excess of quick assets over his current liabilities on open accounts, short-term notes or otherwise." In other words it was not necessary that the specific funds received from the discount of particular paper be used for the required purposes if such funds were offset by adequately liquid investments of the kind mentioned. This, it will be recalled, is in accordance with the recommendation made by the committee to whose report to the Organization Committee reference has already been made.

More significant changes were made by the board in connection with the methods prescribed for determining the eligible

character of paper. The early regulation provided that until January 15, 1915, it would suffice if a proper officer from the bank applying for the rediscount made a statement that "of his knowledge and belief" the original discount was for a purpose contemplated by the law. But it was provided that after January 15, 1915, all paper offered for rediscount must bear on its face, or by indorsement, a statement to the effect that such paper was eligible for rediscount under the regulations of the Board, and must indicate the number of the credit file of the member bank originally purchasing such paper, in which file the member bank held evidence as to the lawful application of the funds advanced. It was also provided that these files should be open for inspection by proper examiners and that copies should be furnished on request to the reserve bank concerned. The regulation also indicated that the information to be found in the file ought to cover "the financial responsibility of the borrower, including a short general description of the character of the business, the balance sheet" as well as profit and loss account. There was also some detailed specification of the items in the balance sheet with the idea of preventing the possibility of a sale of short time paper against slow or permanent investments. Furthermore there was also the requirement that the statement show the maximum aggregate amount up to which the concern supplying the paper expected to borrow, and the regulation stated that such firm ought to obligate itself not to exceed such maximum except with the consent of the member bank with which it was dealing. The regulation finally put the whole responsibility of assuring the lawful character of the paper offered for discount squarely on the shoulders of the member bank. It provided that "the affixing of the stamp stating such paper to be eligible for rediscount will be considered a solemn and binding declaration by the member bank that the statement has been examined from this point of view and that the paper bought complies with all the requirements of the law and of the regulations hereby imposed."

These rather strong requirements were of course never put into effect. Before January 15, 1915, they were suspended, and they were then finally superseded by Regulation 3 of 1915. Moreover, while the method prescribed in the new regulation for certifying the eligibility of paper is more liberal than that in the original reg-

ulation, provision was also made that it should become effective only after July 15.

Under the new regulation a bank applying for a discount must simply certify, over the signature of a duly authorized officer, that to the best of its knowledge and belief the bill was issued for a purpose that made it eligible for rediscount. Instead of *requiring* a credit statement from each borrower the new regulation simply *recommends* one, although in its circular accompanying the regulation the Board strongly urges banks to get their customers into the habit of making statements.

Express provision for the waiving of statements is made in certain cases where bills offered for rediscount were originally discounted by member banks for their depositors. The statement may be waived where the paper is "bona fide two-name" or, as the regulation has it, "if the bill bears the signature of the purchaser and the seller of the goods, and presents prima facie evidence that it was issued for goods actually purchased or sold." The statement may be waived even for single-name paper if, for the depositor concerned, the aggregate amount of obligations actually rediscounted or offered for rediscount does not exceed \$5,000, or 10 per cent of the paid-in capital of the member bank should \$5,000 be in excess of such percentage. Finally the statement may be waived where the bill is secured by an approved warehouse receipt covering readily marketable staples. But where the statement is thus waived the member bank must certify on the rediscount application blank, in whatever manner the reserve bank may require, to the conditions underlying the transaction. The regulation further requires that member banks certify on their letters of application for rediscount whether the paper offered be depositor's paper or purchased paper (paper bought from note brokers), or paper rediscounted for other member banks and whether statements are on file. Where statements are not on file the reserve banks must assume responsibility as to the character of the paper, and in the exercise of this responsibility the reserve banks must get any information necessary from the member banks.

It would thus appear that a member bank is responsible in first instance for the proper application of the proceeds of a bill offered for rediscount. The member banks are urged to keep credit files in all cases so that adequate statements rendered by their clients may be

kept on reference. The board evidently intends that these statements shall be required in the case of rediscounted paper bought from bill brokers and in the case of single-name paper offered for rediscount where the amount exceeds 10 per cent of the paid-in capital of the reserve bank or an absolute amount of \$5,000 should such sum exceed 10 per cent of the capital. Where statements are not required the responsibility of determining the character of the paper rests on the reserve banks themselves, and where the statements are specifically waived the conditions on which they are waived must be certified to the satisfaction of the reserve bank by the member bank offering the paper.

One further point must be made in this connection. Section 14 of the Federal Reserve Act permits the reserve banks under regulations prescribed by the board to purchase and sell in the open market "cable transfers, bankers' acceptances and bills of exchange of the kinds and maturities by this Act made eligible for rediscount with or without the indorsement of a member bank." The question naturally arose as to the meaning of "bills of exchange" in this clause. In a letter sent under date of October 8, 1915, the board answered this question. It held that Congress wished to draw a distinction in section 13 and 14 between the different forms of commercial paper, making "notes, drafts and bills of exchange" of the proper character and maturity eligible for rediscount, but excluding "notes and drafts" from the open market operations. Hence the board held that "promissory notes, even though bearing an additional indorsement, must be regarded as excluded from open market purchases." This therefore precludes the purchase by the reserve banks of single-name paper unless it is offered for rediscount under section 13 and carries a member bank's indorsement.

Trade Acceptances

The Reserve Board, as has been seen, made no secret of the fact that it desired to see the development in the United States of a two-name paper comparable with the bills that grow out of trade acceptances in Europe. Most students have recognized that the establishment and maintenance of an open discount market in the United States would be impossible without a large and steady volume of such paper. Hence it was to be expected that as soon

as it deemed wise the Reserve Board would make some special provision for trade acceptances.

The subject was specifically dealt with for the first time by the Reserve Board in Circular No. 16 and Regulation P, series of 1915, issued July 15, 1915.

In its circular the board states that "trade acceptances" constitute a distinct class of commercial paper, and indicates its readiness to approve for such paper "a rate somewhat lower than that applicable to other commercial paper." In this way the Board believes that it will assist "in developing a class of 'double-name' paper which has shown itself in so many countries a desirable form of investment and an important factor in modern commercial banking systems."

The regulation concerning trade acceptances is divided into three parts, dealing respectively with definition, with character of the paper eligible and with the method of certifying eligibility. The trade acceptance is defined as a bill of exchange

drawn to order and having a definite maturity and payable in dollars in the United States, the obligation to pay which has been accepted by an acknowledgment, written or stamped and signed across the face of the instrument, by the company, firm, corporation or person upon whom it is drawn; such agreement to be to the effect that the acceptor will pay at maturity according to its tenor, such draft or bill without qualifying conditions.

A trade acceptance to be eligible for rediscount must bear the indorsement of a member bank, accompanied by waiver of demand notice and protest; it "must have a maturity at time of discount of not more than 90 days" and it "must be accepted by the purchaser of goods sold to him by the drawer of the bill, and the bill must have been drawn against indebtedness expressly incurred by the acceptor in the purchase of such goods." In other words it is only where the trade acceptance grows out of the actual sale and purchase of goods that it becomes eligible for rediscount. Accommodation drafts, etc., are excluded. In rediscounting a trade acceptance the reserve bank must be satisfied that it was properly drawn, and the necessary evidence to that effect must appear on its face or be supplied in the form of a supplementary certification. But the reserve bank may at its discretion inquire into the nature of the transaction underlying the acceptance.

Commodity Paper

Commodity paper like trade acceptances was encouraged by the Reserve Board in Regulation B, series of 1915, previously discussed. In this regulation the requirement of a financial statement from the borrower offering proper commodity security was specifically waived, but in Regulation 1, series of 1915, issued September 3, 1915, the Reserve Board provided for preferential rates for commodity paper. In explaining the regulation in Circular 17 which accompanied it the board expressed the belief that "this new class of paper with its special rates will prove of particular efficacy in meeting the seasonal demands for credit facilities in the crop-producing districts."

The board defined commodity paper as "a note draft or bill of exchange secured by warehouse terminal receipts, or shipping documents covering approved and readily marketable, non-perishable staples, properly insured." Besides requiring that the paper comply with the statutory demand as to indorsement and maturity, the board fixed the maximum interest that might be charged. It did this by including in the regulation the statement that eligible paper is that (meeting the other requirements) "on which the rate of interest or discount, including commission charged the maker, does not exceed 6 per cent per annum." The significance of this is obvious. Moreover in its circular the board said that in authorizing special rates it would "rely on the federal reserve banks to adopt a policy which will result in securing for the ultimate borrowers the extension of credit on moderate terms by member banks." It suggested the possibility of a discrimination in rate as between trade acceptances and commodity paper but it left the determination of this question to the several reserve banks. The board also left to the reserve banks the preparation of such regulations covering warehouse receipts, etc., as the needs of the several districts might require.

This regulation gives the farmer of the United States a chance to borrow on his garnered crops as he never could before. Moreover the limitation of the interest charged is of more than passing significance. Nothing of this kind has probably happened in the United States before. Moreover, at the time the "commodity paper" regulation was promulgated the Secretary of the Treasury made special deposits of government funds in the reserve banks in

the South. Had the Reserve Board not coöperated with the Secretary by limiting the original interest charge in its definition of eligible commodity paper, the Secretary intended to place the deposits directly in the national banks instead of in the reserve banks and to impose the limitation of a 6 per cent rate as a condition of such deposit. While commodity paper is, of course, of great importance, its character is not such as to give it the same broad status in an open discount market that may be claimed for the trade acceptances. The Reserve Board recognized this in suggesting the possibility of different degrees of preference for the two kinds of paper.

Bankers' Acceptances

Section 13 of the Federal Reserve Act permits the reserve banks to rediscount acceptances growing out of exports and imports and bearing the indorsement of a member bank. Section 14 of the act permits the reserve banks under regulations prescribed by the Reserve Board to engage in open market dealings in cable transfers, bankers' acceptances and bills of exchange eligible for discount.

"Trade acceptances," it will be recalled, were defined by the board as a special form of bill of exchange, growing out of the acceptance, by a buyer of goods, of a draft drawn on him by the seller. In other words "trade acceptances" can arise only as between a buyer and seller of goods in a specific exchange transaction. This form of acceptance is looked upon as a desirable substitute for single-name paper and a preferential rate for it was authorized in the hope of hastening its general domestic use. But "trade acceptances" do not come under the "acceptances" specifically provided for in the act under Sections 13 and 14. "Acceptances" that are distinct from "trade acceptances" are those which may arise from transactions not involving directly buyers or sellers of goods. The use of acceptances of this kind is limited by the act to transactions based on exports or imports. Further it would appear that "acceptances" by bankers are subject to the open market dealings without a member bank's indorsement, but acceptances by those other than bankers can be offered for rediscount only with a member bank's indorsement.

The Reserve Board first dealt with the subject in Circular No.

5 and in Regulation D, series of 1915, issued in February. This circular and regulation were superseded in April by Circular No. 11 and Regulation J. The superseding circular and regulation were made necessary by the fact that Congress had amended the Reserve Act to increase the amount of "acceptances" that member banks might undertake, and also the amount that reserve banks might rediscount. Furthermore, the newer regulation permitted a banker to originate an "acceptance" as well as to receive one, and, where goods were to be released before a bill was paid, permitted the substitution of adequate security for the goods which originally represented the "actually existing values" against which the bill was drawn. In other respects the two sets of circulars and regulations were substantially identical.

In the circular the board discussed the general aspects of the acceptance business. It referred to the newness of the business in the United States but predicted for it a certain development. Hence while it considered that priority should be given to the rediscount of acceptances with the indorsement of a member bank, as provided in section 13, it declared its unwillingness to restrict the business to that field. The position of the acceptance in the world discount market induced the board to permit the reserve banks considerable latitude in the fixing of rates for acceptances, but the board declares it to be in harmony with the spirit of the act to accord preferential rates to acceptances bearing member banks' indorsements. Furthermore it urges upon the reserve banks that when acceptances bearing member banks' indorsements are not available in adequate amounts or on satisfactory terms, the effort should be made to get acceptances bearing a responsible signature of some person other than the drawer and the acceptor and preferably that of a bank or banker. In other words, the board considered it desirable, wherever possible, to have a banker's name on the acceptance.

In the regulation the board established the basis on which the eligibility of acceptances for rediscount at the rates for bankers' acceptances was to be determined. In the first place the acceptance must have been made by a bank (member or non-member), by a trust company, or by some person or firm engaged in the business of accepting or discounting. It must not have been drawn or renewed after surrender of goods to purchaser. In the second place it must

bear on its face satisfactory evidence that it originated in a bona fide export or import sale. Thirdly, where the acceptance is by a "banker" other than a member bank, the acceptor must have agreed in writing to furnish the reserve bank of the district concerned with information concerning the nature of the transaction out of which the acceptance grew. Furthermore, in view of the limitations of the maximum amounts of acceptances prescribed by the act itself, the board rules that a banker's acceptance may be considered as drawn in good faith against actually existing values when the acceptor is secured by a lien on, or by transfer of title to, the goods to be transported; or, in case of release of the goods before payment of the acceptance, by the substitution of other adequate security. The total amount of such acceptances by a single "banker" purchased by a federal reserve bank was in no case to exceed 25 per cent of the paid-in capital of the reserve bank, and, in the case of bills unsecured by liens, by transfer of title or by other acceptable security, the maximum is 5 per cent of such paid-in capital.

The acceptances acquired from member banks under section 13 must naturally bear the indorsement of the member bank. As already indicated, those acquired in the open market need not have a member bank's indorsement, but where an acceptance lacks such indorsement the regulation provides that it shall not be purchased by a federal reserve bank unless the reserve bank has secured a satisfactory financial statement of the acceptor in a form approved by the board.

In Regulation K issued concurrently with Regulation J in April, the board laid down the general conditions according to which a member bank may obtain permission to accept up to the full amount rather than up to simply half of its capital and surplus. According to this regulation, a bank must first make application to the reserve bank of its district which must report on the standing of the applicant and upon the general needs in the district for the service. Each applicant must have an unimpaired surplus of not less than 20 per cent of its paid-in capital, and before it can begin the acceptance business its application must be approved by the Reserve Board. It is apparent from this regulation that it is the purpose of the board to establish firmly at the outset the quality of American acceptances in so far as the board's power and influence may accomplish this purpose.

In the May *Federal Reserve Bulletin* (page 52) the board spoke very hopefully about the actual development of the acceptance business. It referred to the growing appreciation of the acceptance as a credit instrument and to the broadening of the facilities offered by banks for this purpose. A stable acceptance market depends, the board said, on a large steady volume and low steady rates. The board also reported that reliable firms were beginning to quote "forward rates" so that exporters abroad could calculate the relative value of "sterling" and "dollar" acceptances. This, said the board, is of

fundamental importance in the development of the acceptance business. When the movement of our exports and imports has been sufficiently standardized through bankers' acceptances, so that it may be facilitated as easily in the New York market as in the London market even though the volume in the New York market may be much smaller, we should be enabled readily in the future, when we wish to protect our reserves or when they are needed for domestic expansion or seasonal movements of commodities, to deflect the financing of our foreign trade from New York to London by raising New York rates above London rates and making it cheaper for the shipper to draw on London than on New York. Conversely when we are ready to finance it again we should be able, in normal times, to recover the business from London by reducing our rates below those of London.

By September the development of the acceptance business had reached a point where the board felt that further extension might safely be provided for. Under date of September 7 the board issued a new circular and regulation covering the subject. The important changes made were in the section of the regulation dealing with eligibility. In the earlier regulation the renewal of a bill after the goods had been released to the purchaser was forbidden. Under the new regulation renewal is permitted "for such reasonable period as may have been agreed upon at the time of the opening of the credit . . . provided that the bill must not contain or be subject to any condition whereby the holder thereof is obligated to renew the same at maturity." Furthermore the definition of "actually existing values," as found in the clause which specifically exempts from the limitations imposed on other acceptances, bills drawn against "actually existing values," was broadened. The clause "in case of release of goods before payment of the acceptance" was omitted, and the definition was then made to cover all acceptances secured by a lien or by the transfer of title of the

goods to be transported and also acceptances secured simply "by other adequate security." Finally, instead of limiting at a fixed rate of 5 per cent of the paid-in capital of a reserve bank the amount of acceptances *drawn* by a single drawer and discounted by a federal reserve bank, and at a fixed rate of 25 per cent of such capital the acceptances *accepted* by a single firm and discounted at the reserve bank, the Board declared simply that it will from time to time fix the percentage. This obviously provides a much more elastic arrangement.

In Circular No. 19 and in Regulation S, series of 1915, and issued November 29, the Board broadened the acceptance business even more. The new circular and regulation supersede Regulation R issued in September in so far as the September regulation deals with the open market purchases of acceptances under section 14 of the Reserve Act. The new regulation does not bear on the purchases or re-discount of acceptances under section 13 of the act.

The essence of the November regulation is the broadening of the definition of eligibility so that *domestic* as well as *foreign* acceptances may be purchased in the open market by reserve banks. Such domestic acceptances are authorized by the laws of some of the states, and in its circular the board stated that it did not feel justified "when admitting state banks and trust companies into the Federal Reserve system, in stipulating that such domestic acceptances should not be continued under reasonable limitations as a part of their business." A distinction is drawn in the regulation between "foreign" and "domestic" acceptances. The general limitations and prescriptions concerning amounts purchased, etc., remain intact. The character of the eligible "foreign" acceptances is not changed. There is introduced merely the definition of the newly eligible domestic paper. This must be based on a transaction covering the shipment of goods, attested by shipping documents, or it must be secured by a warehouse receipt covering readily marketable staples or by the pledge of the goods actually sold. That the acceptance covers such a transaction must be established by evidence borne on its face or submitted in some other satisfactory form.

Summarizing the accomplishments of the board in the broad field of commercial paper we may say that while the board has

recognized the exigencies of the actual credit situation by accepting for rediscount "single-name" paper, it has excluded such paper from the open market operations, and it has endeavored by means of statements, etc., to safeguard its general character. But in addition to insuring the character of single-name paper rediscounted by the reserve banks, it has sought in the form of "trade acceptances," for which it authorized preferential rates, to encourage the development of a satisfactory two-name paper. To meet the needs of the farmer it has provided preferential treatment for "commodity paper"—although not necessarily on the same basis of preference accorded to trade acceptances. Finally, to supply paper acceptable alike to domestic and foreign bankers, it has made provision for bankers' acceptances, giving an interpretation of the term sufficiently broad to permit the development of "acceptance" firms of the English type. One more important form remains to be developed—the dollar "finance bill." Finance bills in dollars would seem to be precluded by the act itself because such bills are not based on the export or import of commodities, yet the finance bill is necessary to any market aspiring to financial supremacy. Finance bills will be possible, however, only when some provision is made for them through the amendment of the act itself.